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RHEHNSC/NSC WASHINGTON DC  
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RUEHBJ/AMEMBASSY BEIJING 7328  
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UNCLAS SECTION 01 OF 04 SEOUL 000312

SENSITIVE

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SUBJECT: SOUTH KOREA ECONOMIC BRIEFING - FEBRUARY 2010

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In This Issue  
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- Korea Swings to Trade Deficit in January
- Unprecedented Demand for Unemployment Insurance
- ROKG Raises Job Creation Target to 250,000
- Government to Adopt Flexible Hours for Public Sector
- SME Youth Internship Program Resumes in February
- ROKG to Generate 210,000 Local Public Jobs
- Key Interest Rate Remains at Two Percent
- Korea ExIm Bank to Support Export of Nuclear Power Plants
- ROKG to Put Public Debt under Microscope
- Korea's Labor Productivity Ranks 33rd in the World
- Hanwha to Buy Units of Prudential
- Bank Federation Establishes Mortgage Rate Standard
- Attempt to Annul KIKO Contract Ends in Failure
- Banking Industry's Overseas Borrowing Tops USD 2.7 Billion
- Big M&A Deals Increased in 2009
- Bank Earnings Drop 8.6 Percent in 2009
- Kookmin Bank Sells USD 322 Million in Samurai Bonds
- Korean Funds' Asset Value at World's 14th Largest
- FX Reserves Keep Rising in January

Domestic Economy  
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12. (SBU) Korea Swings to Trade Deficit in January: For the first time since January 2009, Korea posted a trade deficit due to increased spending on imports as prices for oil and raw materials rose. The deficit amounted to USD 460 million, a turnaround from the USD 3.09 billion surplus reported the previous month. According to the Korea Customs Service, exports amounted to USD 31.01 billion last month, up 46.7 percent from a year ago, driven by brisk sales of semiconductors and display devices. Imports also grew 26.4 percent to USD 31.47 billion per month due to higher oil and raw material prices. (Yonhap News, February 13, 2010)

13. (SBU) Unprecedented Demand for Unemployment Insurance: The Ministry of Labor said on February 7 that the number of new applicants for unemployment compensation reached a record high of 139,000 in January, rising by 11,000, or 8.6 percent, from a year earlier. It is likely that the end of the government's temporary job-creation projects and seasonal factors contributed to this

surge. Applications grew the most in the public and social welfare sectors and for job seekers in their 50s. The unemployment rate also went up to five percent, the highest since March 2001. (SERI Korea Economic Trends, February 8, 2010 and Yonhap News, February 11, 2010)

14. (SBU) ROKG Raises Job Creation Target to 250,000: At its first National Employment Strategy Meeting on January 21, the government raised its 2010 job growth goal to 250,000 from its previous target of 200,000. The targeted employment rate also increased 0.1 percentage point to 58.7 percent as the government plans to bring the employment rate back up in 2010. During the second NES Meeting on February 18, President Lee Myung-bak criticized officials for not having fresh and realistic ideas. He requested officials take a more active role to create new jobs (Yonhap News, February 19, 2010)

15. (SBU) Korean Government to Adopt Flexible Hours for Public Sector: The South Korean government announced it would allow government employees to work at home or propose flexible work schedules as a way to accommodate employees who are also family caregivers. The government will also allow part-time employees who work more than 60 hours a month to qualify for national health insurance and the national pension fund under the same conditions as full-time employees. Implementation of the new policy will vary according to each ministry. (Maeil Business Newspaper, February 18, 2010)

16. (SBU) SME Youth Internship Program Resumes in February: The Ministry of Labor set aside 207.1 billion won (USD 180 million) for

SEOUL 00000312 002 OF 004

youth internship programs at small- and medium-sized companies (SMEs) with a goal of selecting 30,000 participants. Candidates must be 15 to 29 years old (under 32 years old for those who completed their military service) and unemployed. SMEs and non-profit companies and organizations which have five or more regular employees may participate in this government program. Last year, 32,860 youths found internships in 16,508 SMEs through this program. Among the 8,685 people who completed their internship, 81 percent were hired as regular employees. (SERI Korea Economic Trends, February 1, 2010)

17. (SBU) ROKG to Generate 210,000 Local Public Jobs: On February 4, the Ministry of Public Administration and Security announced an integrated plan to create new jobs jointly with relevant government bodies including the Office of the Prime Minister and the Ministry of Labor. The plan aims to hire 100,000 for "The Hope and Work Project," the government's employment program for low-income workers. The program will create 30,000 jobs in community projects, 3,500 in community business, 13,000 as administrative interns and 63,500 in other public projects. The government agreed to establish committees in each local and metropolitan government and to establish local job centers in major cities with a population of over 500,000. There will be government incentives of 20 billion won (USD 18 million) to encourage competition between local governments. (Maeil Business Newspaper, February 5, 2010)

18. (SBU) ROKG to Put Public Debt under Microscope: Vice Strategy and Finance Minister Hur Kyung-wook stated on February 12 that the government will make every effort to curb public enterprise debt, admitting that snowballing public debt has become a major headache for the Korean economy. Over the years, public firms have become saddled with debt as they have been mobilized to undertake a number of state development projects on behalf of the government. For example, the government last year ordered the Korea Water Resources Corporation to spend 8 trillion won (USD 6.3 billion) to refurbish the nation's four major rivers and 2.1 trillion won (USD 1.6 billion) to build a canal linking Seoul and Incheon. (Korea Times, February 12, 2010)

19. (SBU) Korea's Labor Productivity Ranks 33rd in the World: The Korea Productivity Center announced on February 11 that the nation's labor productivity or value created per worker, averaged USD 42,373 from 2000 through 2007, ranking 33rd among 131 countries. Luxembourg topped the list with each worker producing goods and services worth

USD 89,233, followed by the United States at USD 73,875 and Norway at USD 73,703. (Korea Times, February 11, 2010)

## Finance and Structural Policies

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¶10. (SBU) Key Interest Rate Remains at Two Percent: Meeting on February 11, the Bank of Korea (BOK) rate committee decided to hold its key interest rate at two percent on February 11. The Bank of Korea (BOK) said its rate committee decided to maintain loose monetary policies in order to "sustain" the nation's fledgling economic recovery. Although the economy has been showing signs of improvement, the BOK pointed to recent retrenchment moves in China and the U.S., debt problems in Europe and an uptick in inflation. Citing household debt and inflationary pressures, BOK governor Lee Sung-tae told lawmakers on February 17 that the central bank would not maintain the record-low interest rates much longer. Governor Lee's term ends in March. (JoonAng Daily, February 12 & 17, 2010)

¶11. (SBU) Korea ExIm Bank to Support Export of Nuclear Power Plants: At a meeting with reporters on February 9, Export-Import Bank of Korea chairman Kim Dong-soo said he will form a lenders' group in the first quarter to facilitate export financing for nuclear power businesses. He anticipated total financial support for the consortium will be USD 9.3 billion, roughly 50 percent of the total contract. A consortium led by the Korea Electric Power Corporation won a USD 18.6 billion contract last December to build nuclear power plants in the United Arab Emirates. (Asia Today, February 10, 2010)

¶12. (SBU) Hanwha to Buy Units of Prudential: Hanwha Securities Corporation signed an agreement on February 12 to buy the Korean brokerage and asset management units of U.S. insurer Prudential Financial Inc., a deal estimated to be worth as much as 490 billion

SEOUL 00000312 003 OF 004

won (USD 425.4 million). Hanwha announced it closed the deal to buy a 100 percent stake in Prudential Investment & Securities Corporation and a 99.8 percent interest in the Prudential Asset Management Corporation. (Yonhap News Agency, February 13, 2010)

¶13. (SBU) Bank Federation Establishes Mortgage Rate Standard: The Korea Federation of Banks announced on February 16 a new standard for mortgage rates, Cofix (cost of fund index). The Cofix was created to provide banks with an alternative to the certificate of deposit rate, previously the only benchmark available. The first Cofix rate was set at 4.11 percent for outstanding loans and 3.88 percent for new loans. With the Bank of Korea expected to raise the base interest rate later this year, many borrowers are expected to switch from current CD-based loans to Cofix-based loans. (JoongAng Daily, February 17, 2010)

¶14. (SBU) Attempt to Annul KIKO Contract Ends in Failure: The Seoul Central District Court on February 8 ruled in favor of defendants Woori Bank and Citibank Korea in a lawsuit filed by Soosan Heavy Industries to nullify currency option contracts with the lenders related to the derivative products. This marks the first ruling in a lawsuit between companies and commercial banks on knock-in knock-out (KIKO) products; this ruling stands to have a significant influence on approximately 100 other lawsuits filed by various small and mid-sized companies. (Maeil Business Newspaper, February 9, 2010)

¶15. (SBU) Banking Industry's Overseas Borrowing Tops USD 2.7 Billion: The Financial Supervisory Commission (FSC) reported on February 17 that South Korean banks' mid- to long-term borrowing between January 1 and February 10 this year stood at USD 2.74 billion compared with a monthly average of USD 1.06 billion in the fourth quarter of 2009. Although one-year term spreads rose from 0.67 percent to 0.86 percent in January 2010, spreads with a five year maturity plummeted to 1.55 percent, about the level before the collapse of Lehman Brothers. As the U.S. and Europe confront fiscal deficit issues, the FSC explained that investors are considering Asian markets such as South Korea as comparatively safe investments. (Maeil Business Newspaper, February 18, 2010)

¶16. (SBU) Big M&A Deals Increased in 2009: According to the Fair Trade Commission (FTC), mergers and acquisitions (M&As) totaled 150 trillion won in 2009, up about five percent from 2008. Notably, M&As of large conglomerates increased 33 percent to 16.9 trillion won (USD 13.2 billion). Most M&A activity did not involve business expansion; rather, most of the growth was in mergers of affiliates made for the purpose of management efficiency, the FTC said. (SERI Korea Economic Trends, January 21, 2010)

¶17. (SBU) Banks' Earnings Drop 8.6 Percent in 2009: On February 18, the Financial Supervisory Service (FSS) stated that 18 local banks recorded a combined net profit of 7.1 trillion won (USD 5.56 billion) last year, 8.6 percent less than the previous year. Amid a drop in market interest rates, the net interest margin (NIM) slid 0.33 percentage points last year to 1.98 percent, pulling down interest profit 2.3 trillion won (USD 1.8 billion) to 32.2 trillion won (USD 25.2 billion). However, with improving market rates from the second half of last year, NIM for Q4 last year climbed to 2.33 percent, and interest profit increased 1.5 trillion won (USD 1.2 billion) from the previous quarter to 9.3 trillion won (USD 7.3 billion). (Maeil Business Newspaper, February 19, 2010)

¶18. (SBU) Kookmin Bank Sells USD 322 Million in Samurai Bonds: South Korea's Kookmin Bank has become the first Asian private institute to issue yen-denominated "Samurai bonds" after the bankruptcy of Lehman Brothers. Kookmin Bank sold about USD 322 million worth of the two-year bond and will use the funds raised to redeem Samurai bonds maturing in April. (Maeil Business Newspaper, January 28, 2010)

¶19. (SBU) Korean Funds' Asset Value at World's 14th Largest: The net asset value of South Korean funds in the third quarter last year was USD 268.9 billion, 5.6 percent higher than the end of previous quarter, and amounted to the world's 14th largest. According to a report released by the Korea Financial Investment Association on January 27, the net asset value of global funds is USD 22.4 trillion, up USD 2 trillion from the end of previous quarter. (Maeil Business Newspaper, January 28, 2010)

SEOUL 00000312 004 OF 004

¶20. (SBU) FX Reserves Keep Rising in January: Korea's official foreign reserves in January 2010 amounted to USD 273.69 billion, an increase of USD 3.70 billion from USD 269.99 billion at the end of the previous month. The BOK attributed the increase to operating profits on foreign reserves and the National Pension Service's redemptions of its mature currency swaps with the Bank of Korea. These transactions offset a decline in the U.S. dollar value of Euro-denominated reserves. (Bank of Korea Press Release, February 2, 2010)

TOKOLA